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No. 475

In the Supreme Court of the United States

October Term, 1944

THE PEOPLE OF [illegible]

v.

[illegible]

ON [illegible]

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In the Supreme Court of the United States

OCTOBER TERM, 1944

No. 475

THE PENFIELD COMPANY OF CALIFORNIA, PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

OPINION BELOW

The opinion of the circuit court of appeals (R. 345) has not yet been officially reported. The district court rendered no opinion.

JURISDICTION

The judgment of the circuit court of appeals was entered on June 30, 1944 (R. 360–361), and rehearing was denied on August 8, 1944 (R. 361). The petition for a writ of certiorari was filed on September 16, 1944. The jurisdiction of this Court is invoked under Section 240 (a) of the

Judicial Code, as amended by the Act of February 13, 1925, which is made applicable by Section 22 (a) of the Securities Act of 1933.

QUESTION PRESENTED

Whether the court below properly affirmed a district court order enforcing a subpoena *duces tecum* issued by officers of the Securities and Exchange Commission in connection with an investigation into suspected violations of the Securities Act of 1933.

STATUTE INVOLVED

The applicable provisions of the Securities Act of 1933 (15 U. S. C. 77a *et seq.*) are set forth in the Appendix, *infra,* pp. 10–12.

STATEMENT

Pursuant to Section 20 (a) of the Securities Act (15 U. S. C. 77t (a)), the Commission is conducting an investigation to determine whether petitioner and other specified persons have violated Sections 5 (a) and 17 (a) (15 U. S. C. 77e (a) and 77q (a)) by selling petitioner's stock and securities consisting of whiskey-bottling contracts without registration and by means of untrue statements of material facts (R. 8–15). The investigation was instituted by order of the Commission upon information tending to establish certain facts, recited in the order, which indicated that petitioner and others had violated the Act (R. 8–15). In this order (and in a subsequent supplemental order) the Commission empowered cer-

tain of its officers "to administer oaths and affirmations, subpoena witnesses, compel their attendance, take evidence, and require the production of any books, papers, correspondence, memoranda or other records deemed relevant or material to the inquiry" (R. 11, 15). Accordingly, one of the designated officers directed a subpoena to petitioner requiring it to produce certain of its books, papers, and documents which are specifically itemized (R. 15–18).

Petitioner failed to comply with the subpoena and the Commission applied to the district court for its enforcement (R. 2–19) pursuant to Section 22 (b) of the Act (15 U. S. C. 77v (b)). The Commission showed that purchasers of whiskey warehouse receipts from petitioner or from another company under investigation, Bourbon Sales Corporation, had been induced to turn over the receipts to petitioner in exchange for bottling contracts or stock; that the bottling contracts had been offered or sold through the mails on the representation that the only way the receipt holders could earn a profit would be by utilizing the facilities of Bourbon Sales Corporation or petitioner enabling those companies to bottle and sell the investor's whiskey with minimum expense and at the highest price; and that petitioner's stock had been sold through the mails by means of literature which omitted to state its true book value and contained misrepresentations concerning petitioner's profit potentialties (R. 160, 162, 190–193, 201–204, 340, 342).

The district court granted the Commission's application, specifically ordering the petitioner to produce all the items, twenty in number, which were enumerated in the subpoena (R. 311, 313–316). The circuit court of appeals affirmed (R. 344).

ARGUMENT

1. Presumably on the theory that certain of the items in the subpoena related only to the whiskey bottling contracts and not to the sale of its stock, petitioner asserts that there is error in the determination that these contracts are securities within the meaning of Section 2 (1) of the Act (15 U. S. C. 77b (1)).[1]

This determination by the circuit court of appeals (not by the district court, as stated by petitioner (Br. 19)), was not necessary to the decision. Examination of the face of an instrument is not always sufficient to determine whether it is a security within the meaning of Section 2 (1) of the Act. The "plan of distribution, and the economic inducements held out to the prospect" are material considerations in such a determination. *Securities and Exchange Commission* v. *C. M. Joiner Leasing Corp.*, 320 U. S. 344, 353. The Commission could properly inquire into the circumstances of the issuance and sale of

[1] Petitioner argues also that the district court erred in holding that the warehouse receipts (as distinguished from the bottling contracts) were securities (Br. 20). No such holding was made by either court below and the Commission has expressed no opinion as to whether the whiskey warehouse receipts, standing alone, are securities.

the bottling contracts in order to elicit facts indicating whether they constituted securities within the purview of the Act. The Commission is entitled to the enforcement of any subpoena which is "not plainly incompetent or irrelevant to any lawful purpose" in the discharge of its duties under the Act. *Endicott-Johnson Corporation* v. *Perkins,* 317 U. S. 501, 508–509. In the light of the *Joiner* case, *supra,* it is clear that the subpeona complied with this standard.

Moreover, the determination of the court below that the bottling contracts are securities is correct. Persons who had previously purchased whiskey warehouse receipts were offered and sold these contracts upon the representations that petitioner or Bourbon Sales Corporation would take care of all details in taking the whiskey out of bond, bottling it and selling it, and would see that the investor received a profit (R. 86, 88–89, 160, 162, 190–193, 201–204, 340, 342). The contract holders were to do nothing; indeed, they did not have the facilities or the necessary federal and state liquor licenses (R. 96, 166) to take the whiskey out of bond and dispose of it. Petitioner represented that there would be a pooling of the whiskey it purchased from various receipt holders (R. 159–160) so that, under the scheme, each contract holder would get no more than a right to share in the avails of a mass of whiskey processed by petitioner. Under these circumstances, the bottling contracts fall within the

statutory definition of Section 2 (1), which specifically includes as a "security" any "certificate of interest or participation in any profit-sharing agreement," any "investment contract," and "any interest or instrument commonly known as a 'security.'" The record makes clear that the entire scheme involved, in substance, a speculative investment in a common enterprise necessarily contemplating complete reliance by the investor upon the efforts of the seller. The bottling contracts were given the character of securities by "the terms of the offer, the plan of distribution, and the economic inducements held out to the prospect." *Securities and Exchange Commission* v. *C. M. Joiner Leasing Corp.*, 320 U. S. 344, 352–53.

2. Petitioner urges that under Section 19 (b) only those books, papers and documents which the Commission itself has found relevant or material to the inquiry may be subpoenaed, and that no such finding was made in this case. It should first be noted that when the Commission authorized these enforcement proceedings to be taken, it did pass on the relevancy and materiality of the documents sought (R. 5). Thus, petitioner ultimately received the benefit of the Commission's judgment to which it contends it is entitled.

In any event, the court below properly held that under Section 19 (b) the determination as to what books, papers, or other documents are relevant

and material to the inquiry may be delegated to the officers designated by the Commission to conduct the investigation. *Woolley* v. *United States,* 97 F. (2d) 258, 262 (C. C. A. 9), certiorari denied, 305 U. S. 614. See also H. Rep. No. 85, 73d Cong., 1st sess., p. 25. The Commission itself, of course, formally decides that the facts in its possession warrant an inquiry to determine whether the Act has been violated. And the statutory provision authorizing the Commission to delegate its subpoena powers, which was recognized by this Court in *Cudahy Packing Co.* v. *Holland,* 315 U. S. 357, 365, would be eviscerated were the officers to whom the power was delegated nevertheless required thereafter to return to the Commission for a decision as to the relevancy and materiality of the documents to be subpoenaed. There is no warrant for saying that the delegation authorized by Section 19 (b) is merely the delegation of the purely ministerial and mechanical functions involved in the issuance of a subpoena. To so hold would be inconsistent with the provision relating to the appointment of examining officers and would seriously hamper effective administration. The delay which would necessarily result from such an interpretation of Section 19 (b) would be particularly injurious in view of the three-year period of limitation (Act of December 27, 1927, 45 Stat. 51, 18 U. S. C. 582) on criminal prosecutions under the Securities Act (Sec. 24; 15 U. S. C. 77x).

3. Petitioner asserts finally that the order enforcing the subpoena authorizes an unlawful seizure contrary to the Fourth Amendment, and that the provision of Section 19 (b) of the Act giving the Commission power to issue a subpoena *duces tecum* is a delegation of judicial power in violation of Article III of the Constitution.

The short answer to this latter argument is to be found in its rejection by this Court, fifty years ago, in *Interstate Commerce Commission* v. *Brimson,* 154 U. S. 447, 476.

As to the "search and seizure" argument, the Fourth Amendment requires only that the demand be reasonably specific and limited to documents relevant to the inquiry. *Wilson* v. *United States,* 221 U. S. 361, 375–376; *Baltimore & Ohio Railroad Co.* v. *Interstate Commerce Commission,* 221 U. S. 612, 622; *McMann* v. *Securities and Exchange Commission,* 87 F. (2d) 377, 379 (C. C. A. 2), certiorari denied, 301 U. S. 684. Although petitioner speaks of "an arbitrary finding" as to what is relevant and material, it has not attempted to show that any of the twenty items specified in the subpoena is irrelevant or immaterial to the inquiry.[2] Consideration of these items (R. 15–18)

[2] In fact, the only specific criticism which petitioner makes on this score is directed to language which appeared only in the order to show cause (R. 20) and is not found in either the subpoena or the order under review (R. 15–18, 313–316). This language in the order to show cause referred to "All

in the light of the subject of the Commission's inquiry shows that the court below correctly found that "The twenty items of the subpoena are within the normal area of such an investigation" (R. 357).

CONCLUSION

The decision below is correct, and there is no conflict of decisions. The petition for a writ of certiorari should be denied.

Respectfully submitted.

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books, records, documents, contracts, agreements, checks, bank statement, correspondence files and all other papers and memoranda in which have been entered a record of the transactions and business of The Penfield Company of California * * * "from the date of its incorporation to the date of this subpoena" (Br., 21).